

**CITY OF LODI  
INFORMAL INFORMATIONAL MEETING  
"SHIRTSLEEVE" SESSION  
CARNEGIE FORUM, 305 WEST PINE STREET  
TUESDAY, MAY 10, 2005**

An Informal Informational Meeting ("Shirtsleeve" Session) of the Lodi City Council was held Tuesday, May 10, 2005, commencing at 7:01 a.m.

**A. ROLL CALL**

Present: Council Members – Hansen, Hitchcock, Johnson, Mounce, and Mayor Beckman

Absent: Council Members – None

Also Present: City Manager King, City Attorney Schwabauer, and City Clerk Blackston

**B. TOPIC(S)**

B-1 "Review and update regarding Electric Utility issues"

Electric Utility Director Vallow recalled that in 1999 the Utility's capital program was reviewed. The City issued \$42 million (net proceeds) of bonds and the funds were deposited into a capital account held by the trustee Bank of New York. Within the \$42 million was \$12 million to build a 60 kV transmission line from Lodi to White Slough, hooking up to the Western Area Power Administration. The City established a reimbursement resolution in 1997. The first \$6 million of proceeds went to reimburse the City for capital expenses. Refinancing was done in 2002. The City received a lower interest rate and returned \$6 million to lower the debt. Mr. Vallow reviewed the following documents (all filed): 1) Capital expenditures 1999-05; 2) Five year capital plan 2006-10; and 3) a list of projects paid for from the borrowed funds from 1999 to March 31, 2005 with a total cost of \$21,593,942. Approximately \$11.9 million is projected to be in the bond fund at the end of this year and will be spent down in 2005-08. After that time, it is expected that the capital program will be funded 100% from revenues/electric rates. Approximately \$8 million is budgeted in Operations and Maintenance (O&M) of which \$6.5 million is for O&M and \$1.5 million is for capital.

City Manager King reported that the City made the finding, when it offered the bond resolution and indentures, that it could reasonably expend the money in five years. He wants to ensure that the City is spending down the money within the appropriate time period and that it is performing to the list of projects that borrowers were told the City would spend the money on.

Mayor Pro Tempore Hitchcock recalled that previous discussions occurred related to spending the borrowed money on new street lighting. She did not believe it was listed in the original borrowing; however, staff informed her it was for "Dusk to Dawn Lighting". In reviewing the budget it appears that very little money was expended on the Dusk to Dawn Lighting program, yet street lighting costs totaled approximately \$5 million. She pointed out that neither of the major projects for which the money was borrowed have been accomplished, i.e. the 60 kV transmission line and the new Electric Utility building. Ms. Hitchcock asked staff to provide her with the original list of projects that were outlined in first borrowing, so that she could compare it to the list Mr. Vallow presented today.

Mr. Vallow replied that the transmission line project ceased when the energy crisis and Pacific, Gas & Electric bankruptcy occurred.

Jim Pope, General Manager of the Northern California Power Agency (NCPA), stated that he had been asked by the City Manager to look at the financial situation of the Lodi Electric Utility. The Utility's credit rating was downgraded a couple of years ago from A- to BBB+,

which in turn downgraded NCPA's rating. With the aid of overheads (filed), Mr. Pope outlined a list of goals for the Utility. He stated that a plan needs to be developed to accomplish what the rating agencies were told by the Utility in 2002. He recalled that in the late 1990s restructuring was put in place by AB1890, which significantly changed the market and industry and created more risk on customers' power supply cost. Adequate reserves need to be maintained so the Utility can deal with uncertainties and contingencies that come forward in the future. It appears that Lodi Electric Utility has a gap of \$6 million to \$7 million between electric revenues and expenses, which is going to require a rate increase for retail customers over the next several years. There is also concern about the Utility meeting the debt coverage ratio of 110% of debt service coverage. Rating agencies were told that the City would increase rates via Market Cost Adjustments (MCA) to build a cash reserve of \$15 million by 2008. Currently the Utility has a \$6.5 million total cash reserve. Lodi's wholesale power costs do not have an adequate cushion for future power purchases, due to unknown forward market prices. He reviewed projected revenues/expenses for 2005-11 and reported that a shortfall would occur by 2007 and increase in the future. Failure to meet the minimum debt service coverage would mean a technical default, which could possibly cause immediate disclosure to the bondholders, an early call on the bonds, downgrading of the bonds to junk status (i.e. BBB- or C), as well as an impact on the NCPA bond rating. It would negatively affect the Utility's ability to obtain energy in the wholesale energy market. A 25% rate increase would result in a \$15 million reserve by 2009-10. An option would be to increase rates 10% in 2006, 10% in 2007, and 5% in 2008. He explained that a MCA is limited to the energy cost market that the Utility is covering. A full rate increase would cover the cost of energy and other increasing costs such as inflation, contingencies, or building a reserve for capital needs.

Council Member Hansen commented that one of the reasons the Utility finds itself in this situation is that MCAs were not made during a very volatile time period. He felt it was imperative that the Utility's credit rating not drop below B+.

In answer to questions posed by Council, Mr. Pope stated that one way to assure cost certainty is to acquire energy on a longer term basis. For major projects electric utilities can either reserve the money going forward or borrow the money and put the debt service and principal in rates for 30 years. He stated that a distribution substation costs between \$12 million to \$15 million. He reported that all other members of NCPA are rated A- or above.

Council Member Mounce expressed concern that an explanation for the current situation of Electric Utility has not been clearly delineated. She was opposed to increasing electric rates until financial responsibility resumes, and it is determined that prudent management of the Utility has been undertaken.

Addressing Mr. Vallow, Mayor Pro Tempore Hitchcock asked why the rate structure was not sufficient to cover costs of doing business and why Council has not been kept informed of the situation.

Mr. Vallow replied that very few people understood what was going to be happening (to the market) from February to March. For the last several years decisions have been made based on history and it has been the practice to buy out two quarters in advance. Mr. Vallow stated that his mission has been to keep electric rates low. He reported that the strategy undertaken this year has saved a "couple million dollars". Mr. Vallow commented that if there is a policy shift in which rate increases are acceptable in exchange for higher certainty, he would follow it.

Council Member Hansen suggested that it might be beneficial to tier residential rates to minimize the increases. He pointed out that commercial and industrial customers' rates in Lodi are much lower than PG&E, pursuant to Council policy in an effort to attract businesses to the community.

Mr. King reported that he would be centralizing accounting functions by bringing an Electric Utility employee into the Finance Department under the direction of Finance Director Krueger. Checks and balances need to be in place regarding bulk purchase power buying decisions. It is planned to involve the Finance Department, City Manager's Office, and NCPA to a greater degree in making those decisions. In addition to Electric Utility, the City needs to develop healthy reserves in the Water and Wastewater funds to pay for the PCE/TCE contamination cleanup costs.

Mayor Pro Tempore Hitchcock did not think that moving an Electric Utility employee under the Finance Director was a good long term way of handling the situation. Mr. King estimated that it would be necessary for one or two years.

**C. COMMENTS BY THE PUBLIC ON NON-AGENDA ITEMS**

None.

**D. ADJOURNMENT**

No action was taken by the City Council. The meeting was adjourned at 8:37 a.m.

ATTEST:

Susan J. Blackston  
City Clerk

*filed 5-10-05*



# **Electric Utility Department**

## **Capital Overview of the Electric Utility**

City Council  
Shirtsleeve Meeting  
May 10, 2005



# Electric Utility Department

## Capital Expenditures 1999-2005 (Amounts in Thousands)

Initial Bond Proceed 8/31/99: \$42,000,000

	1999	2000	2001	2002	2003	2004	2005	Total
Capital Expenditures	(3,562)	(3,056)	(3,384)	(3,104)	(3,090)	(2,607)	(2,789)	(21,592)
Other Expenditures	*(6,000)			** (6,000)				(12,000)

Projected Balance June 30, 2005: \$11,900,000

\*Reimbursement for capital expenditures 10/1/1991 - 8/1/1999

\*\*Return of proceeds during 2002 re-financing



# Electric Utility Department

## Five Year Capital Plan

### Fiscal Year 2006-2010

(Amounts in Thousands)

	2005/2006	2006/2007	2007/2008	2008/2009	2009/2010	Total
Total Capital Expenditures	3,500	5,500	5,500	4,000	3,500	22,000
Included in O&M Budget (rates)	1,500	1,500	3,000	2,500	2,500	11,000
Net added cost	2,000	4,000	2,500	1,500	1,000	11,000
Funded existing bond proceeds	3,500	5,500	2,900	-	-	11,900
Capital Fund Balance	9,900	5,900	3,400	1,900	900	

00161 Utility Outlay Reserve Fund

Description	1999	2000	2001	2002	2003	2004	2005*	Total by acct
161001 Electric Contingency	-	-	-	-	-	43,781	17,381	61,162
161037 JD Edwards Implementation		119,651	-	-	-	-		119,651
161045 Stockton St/Lodi-Lockefor	-	-	-	10,923	-	-		10,923
161050 Elm St Recon/Church	-	-	-	224,373	-	-		224,373
161052 SCADA & UPS System	-	-	-	82,501	7,000	-		89,501
161062 Stockton St/Tokay to Lodi	-	-	-	86,858	-	-		86,858
161069 Lodi Station Parking Structure	-	-	-	104,027	5,864	-		109,891
161369 Pw-Local Area Network System	4,752	9,434	-	-	-	-		14,186
161392 Wide Area Network	-	45,044	7,465	-	-	-		52,509
161633 Street Light Improvement	-	-	-	-	-	23,412	56,383	79,795
161646 EUIP-EUD Syst Studies	-	-	-	-	22,331	-		22,331
161647 EUIP-Interconnect-Substation	90,527	81,253	30,934	31,248	42,331	4,088	30,477	310,858
161648 Interconnect-Trans Line	147,202	-	3,978	-	-	-		151,180
161649 Interconnect-Misc	293,753	2,391	-	-	-	-		296,144
161650 Electric Service Center	-	226	219	1,196	13,842	45,543	220	61,246
161651 EUIP-Line Extensions	469,465	602,794	933,784	509,731	300,512	451,858	466,230	3,734,374
161652 EUIP-Distribution Systm	973,745	916,399	1,096,427	841,911	996,980	463,869	265,831	5,555,162
161653 EUIP-Service Connections	87,867	172,829	184,547	151,470	105,440	123,167	127,846	953,166
161654 EUIP-Dusk to Dawn Lighting	(1,540)	2,628	685	377	498	1,432	1,582	5,662
161655 EUIP-Substructures	163,848	110,940	188,193	145,992	149,530	263,154	161,687	1,183,344
161656 EUIP-Service Connections	30,452	88,526	41,888	56,580	60,015	73,640	45,713	396,814
161657 EUIP-Substation Const	1,186,116	80,850	57,953	50,840	9,089	257,674	7,699	1,650,221
161658 Substation Const-Protection	15,599	-	-	-	-	-		15,599
161669 Substation Block Wall	-	-	-	6,115	56,728	30,468		93,311
161672 EUIP-Street Light Improve	-	27,383	289,528	625,181	1,198,797	138,860	658,009	2,937,758
161674 Streetlight Standards Upgrade	-	-	-	-	-	3,765	2,384	6,149
161675 EUIP-MSD Expansion	-	51,107	39,518	75,150	-	-		165,775
161677 Killelea Substation Construction						187,590	79,590	267,180
161676 EUIP-Property-E.Lodi Ave	-	38,083	-	-	-			38,083
161679 Operations Ctr Modification	-	-	-	-	-	-	13,916	13,916
161680 EUIP-60KV Line Ind Subs	-	-	134,562	3,081	58,423	35,766	75,814	307,646
161681 EUD Operations Center Improvement	-	-	9,899	2,098				11,997
161682 Remote Radio Meters Project	-	-	-	21,534	4,763			26,297
161685 Fiber Optic System	-	-	-	-	-	379,477	160,334	539,811
164019 LED Traffic Signal	0	91,329	0	0	0	0	0	91,329
1611201 EUIP-Capital Equipment	100,724	615,709	365,253	72,795	58,197	78,501	618,561	1,909,740
Year Total	3,562,510	3,056,576	3,384,833	3,103,981	3,090,340	2,606,045	2,789,657	21,593,942

\* note: 2005 YTD March 31, 2005

Filed 5-10-05

# City of Lodi Electric Utility Department



## Financial Overview Presentation

By Jim Pope

General Manager, NCPA

Prepared by Donna Stevener, AGM/CFO, NCPA

May, 10, 2005



# List of Goals for Lodi Electric Utility

- Develop a financially sound Electric Utility that can contribute to overall city success and provide dividends to customer/owners
- Develop a plan to accomplish what Rating Agencies were told in 2002 – build reserves!
- Develop sound fiscal policies and long-term plans
- Develop long-term power supply plan to obtain cost certainty for customers
- Improve current bond rating
- Develop and maintain adequate reserves
- Balance achievement of above Goals with impacts to customers

# List of Concerns/Issues

## Overall concerns:

- Lodi appears to have a large gap (\$6 to 7+ million) between Electric revenues and expenses which requires rate increases to retail customers over the next several years
- Meeting of debt coverage ratio covenant
- Rating Agencies were told that increased rates via Market Cost Adjustment (MCA) would build cash reserves to \$15 million – currently only \$6.5 million in total cash (3/31/05)

# List of Concerns/Issues

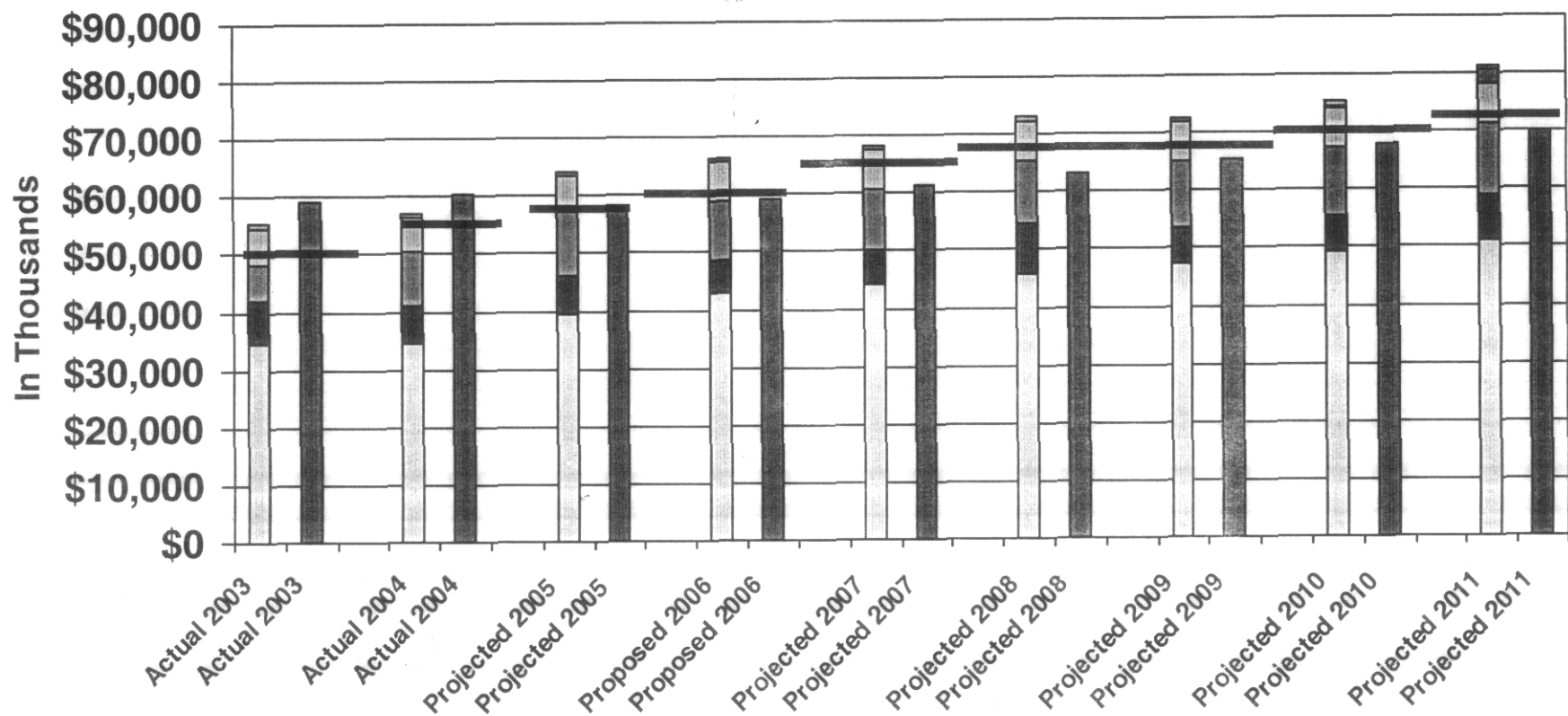
## Overall concerns:

- Power budget may not have adequate cushion for future power purchases due to unknown forward market prices – no price/cost certainty due to unhedged power costs during next year and beyond
- Rating downgrades for Lodi impact NCPA ratings and impact all other NCPA members as well

# Lodi Electric Utility Department Projected Revenues/Expenses

FY ending 2005 to 2011

— Revenues needed to obtain minimum 1.10 debt service coverage



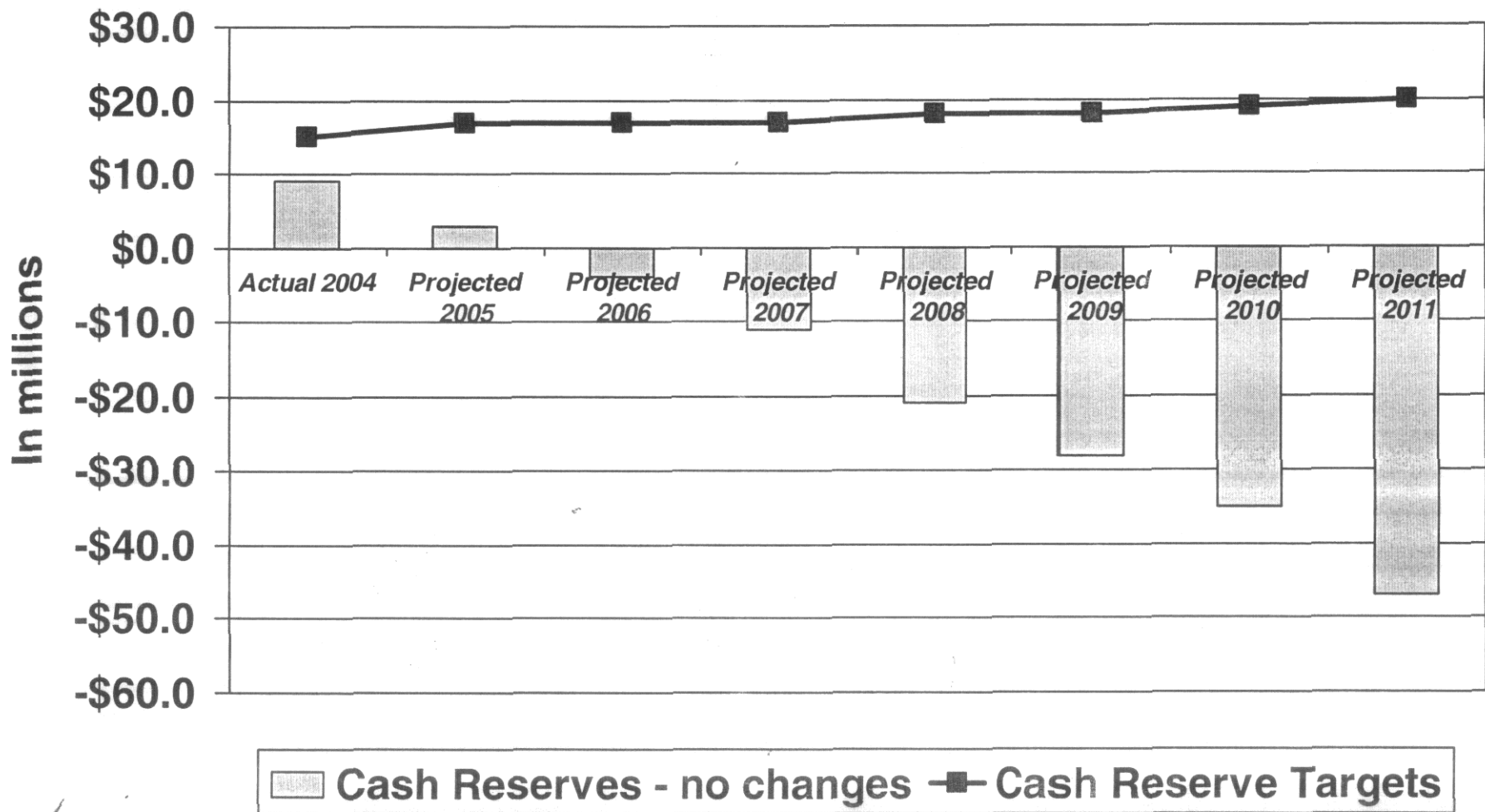
☐ Power Supply  
☐ Operations & Maintenance  
☐ Capital Program  
☐ Total Revenues

☐ Debt Service  
☐ PILOT or transfer to General Fund  
☐ Public Benefits

# Lodi Electric Utility Department

## Projected Cash Balances – Do Nothing Scenario

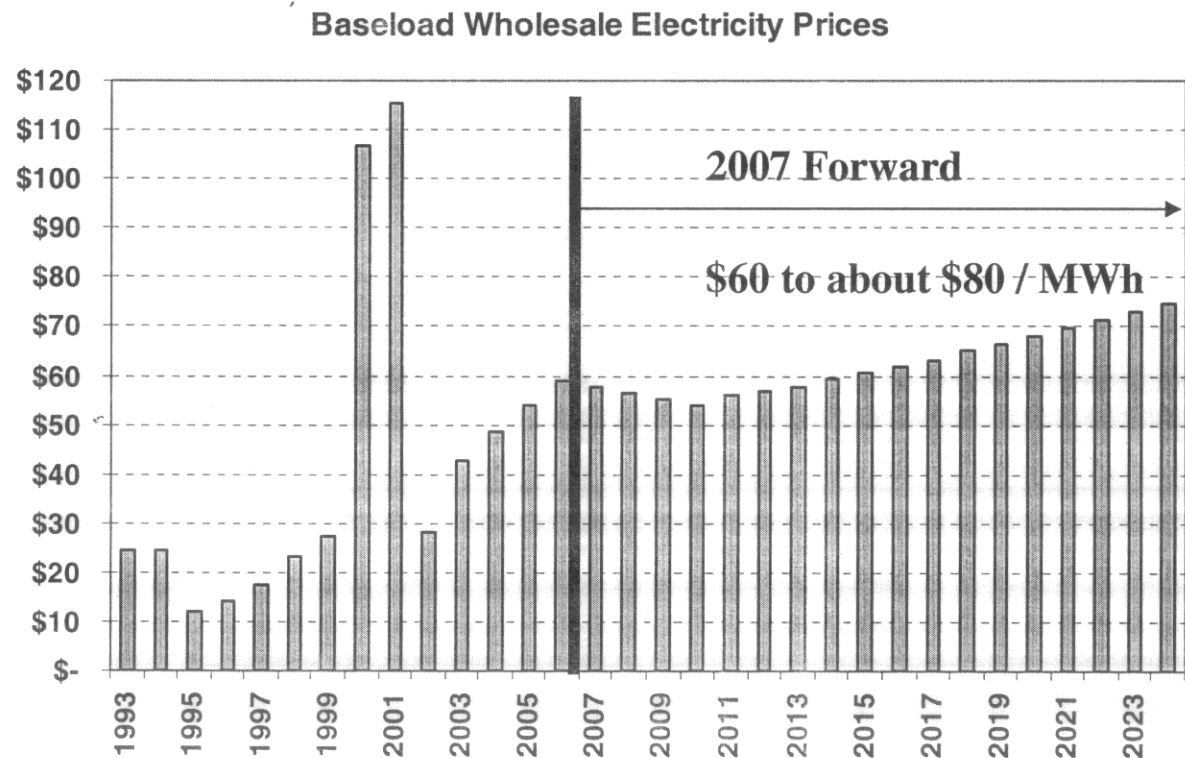
FY ending 2005 to 2011



# What is driving this?

- Purchased power is the main cost driver for the electric utility

**Current and forward purchased power market is very volatile and increasing costs are projected for the future**



# So...Why should we care?

Lodi has agreed in official bond documents to:

## **Rate Covenant**

Pursuant to the 2002 Contract, the City covenants (the "Rate Covenant") that it will at all times fix, prescribe and collect rates and charges for the services, facilities and electricity of the Electric System during each Fiscal Year which will be at least sufficient to yield: (a) Adjusted Annual Revenues for such Fiscal Year at least equal to the sum of the following for such Fiscal Year: (i) Adjusted Maintenance and Operation Costs; (ii) Adjusted Annual Debt Service with respect to the Installment Payments and Parity Obligations, and (iii) all other payments required to meet any other obligations of the City which are charges, liens or encumbrances upon or payable from the Electric Revenue Fund including all amounts owed to any issuer of a Financial Guaranty then in effect and deposited in the Reserve Fund under the terms of such Financial Guaranty; and (b) Adjusted Annual Net Revenues for such Fiscal Year equal to at least 110% of the Adjusted Annual Debt Service with respect to the Installment Payments and Parity Obligations for such Fiscal Year. The City may make adjustments from time to time in such fees and charges and may make such classification thereof as it deems necessary but may not reduce the rates and

charges then in effect unless the Adjusted Annual Revenues and the Adjusted Annual Net Revenues from such reduced rates and charges will at all times be sufficient to meet the requirements described in the preceding sentence.

# What does this mean to Lodi?

- Failure to provide minimum debt service coverage on bonds would mean a technical default on outstanding debt
- Possible consequences –
  - Immediate disclosure to bondholders
  - Early call on bonds
  - Downgrading of bonds to junk bond status
  - Impact on NCPA bond rating as well as fellow NCPA member munis
  - Increased future bond costs for Lodi customers
  - Impact on ability to obtain energy/ increased purchased power costs due to Lodi's counterparty risk

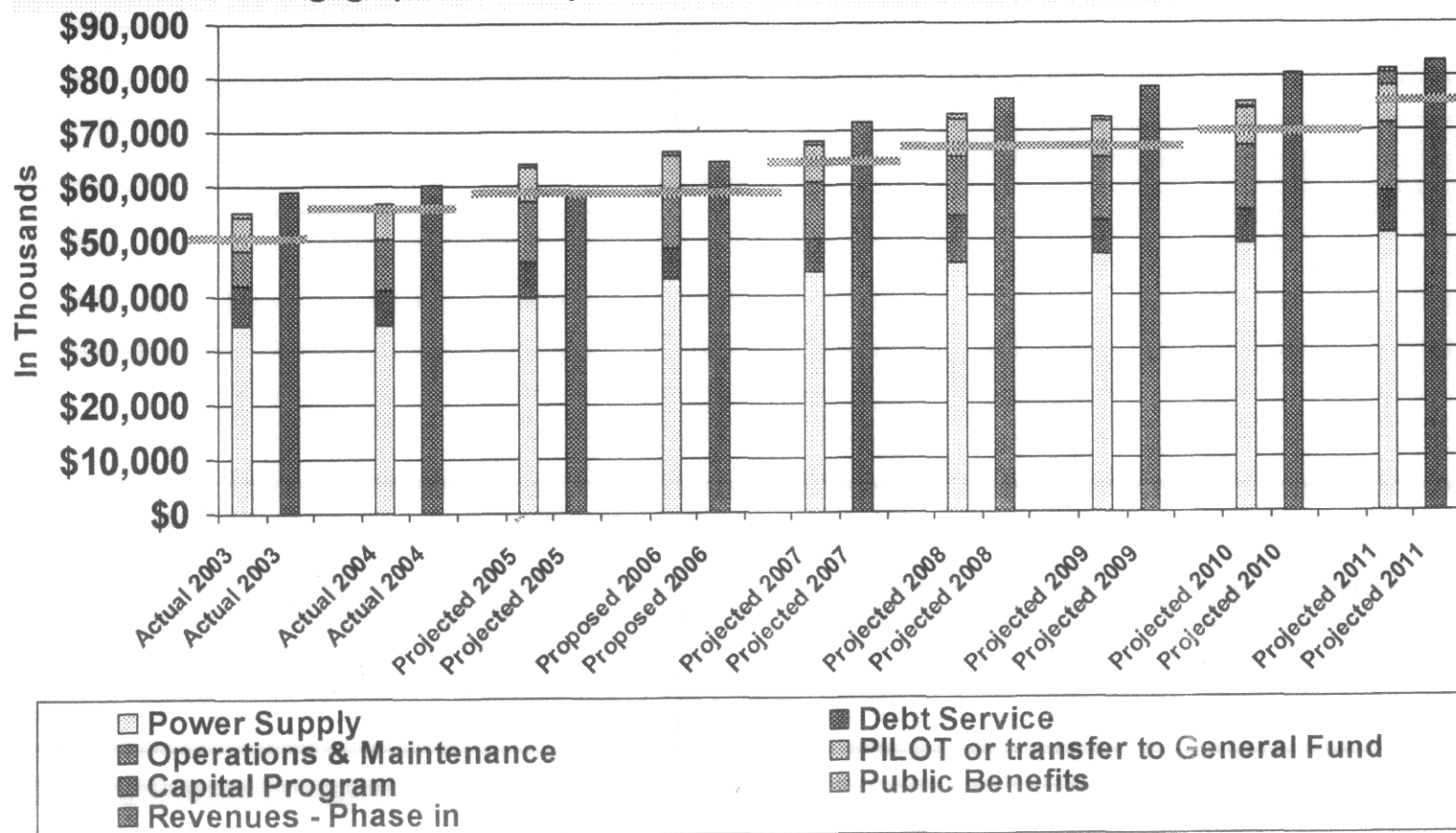


# What should Lodi's picture look like?

## Projected Revenues/Expenses

FY ending 2005 to 2011

Assumed fixing gap over 3 years, plus building reserves



Revenues needed to obtain minimum 1.10 debt service coverage

# Lodi Electric Utility Department Rate Increase Options

## 3 Year Rate/Revenue Increase

- 10% in FY 2006
- 10% in FY 2007
- 5% in FY 2008
- No increase in years 2009 or 2010

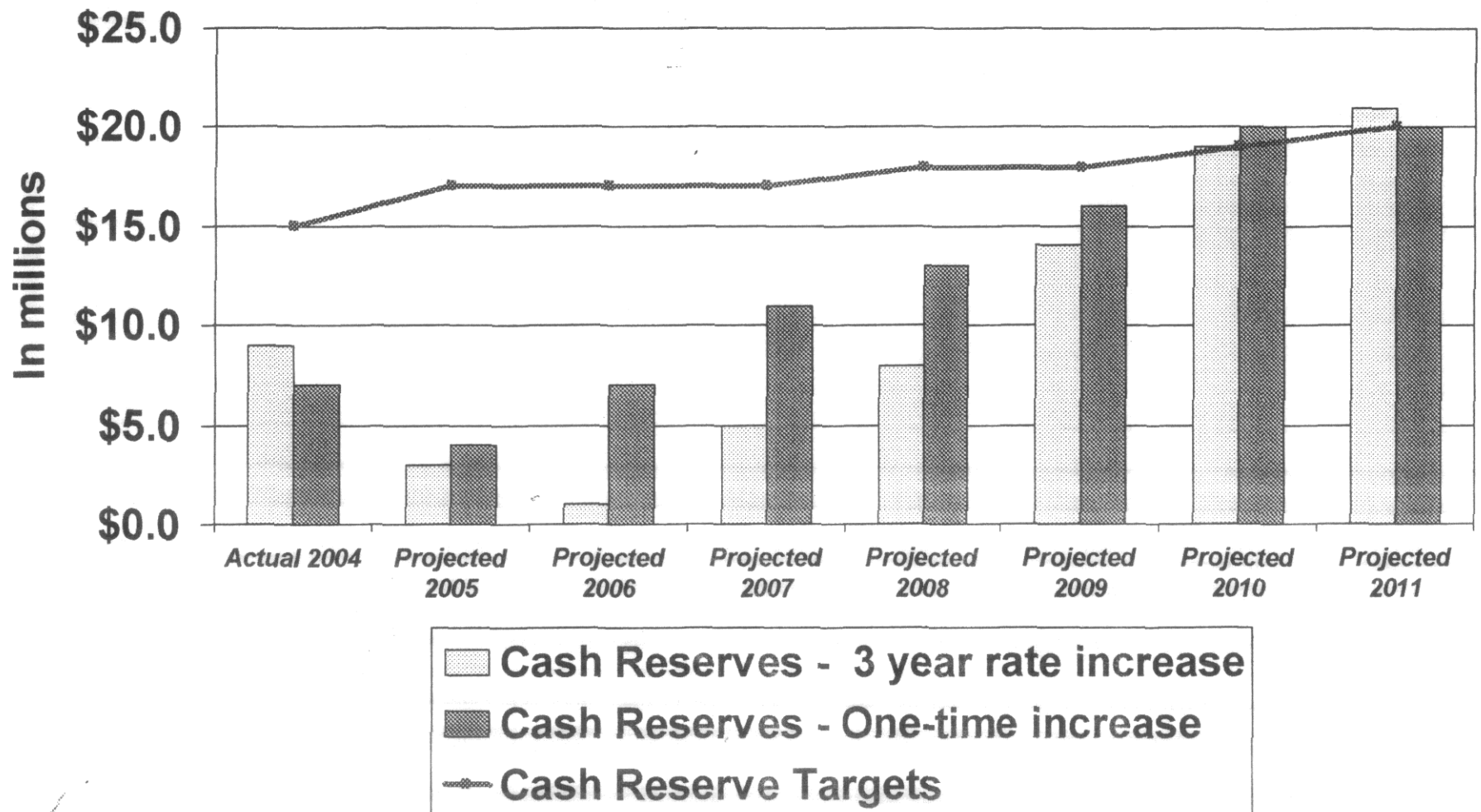
## One-time Rate/Revenue Increase

- 25% in FY 2006
- No increase in years 2007 thru 2010

# Lodi Electric Utility Department

## Projected Cash Balances – Possible Scenarios

FY ending 2005 to 2011



# How do we get there?

## Recommendations by NCPA

	Recommendation
A	Adopt a 3-year rate increase plan as soon as possible
B	Prepare a long-term financial plan (5 years at least)
C	Develop and implement strategies for long-term power needs
D	Adopt a fiscal policy and set specific reserve goals for capital, rate stabilization, energy risk, etc.
E	Prepare a long-term capital plan, including source of funding balanced between rates and bonds

**Thank You**

**Questions?**